

Message Text

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ACTION NEA-12

INFO OCT-01 EUR-25 ISO-00 CIAE-00 DODE-00 PM-07 H-03

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P R 011415Z MAR 74

FM AMEMBASSY NEW DELHI

TO SECSTATE WASHDC PRIORITY 0022

INFO AMEMBASSY COLOMBO

AMEMBASSY DACCA

AMEMBASSY ISLAMABAD

AMEMBASSY KATHMANDU

USMISSION OECD PARIS

AMCONSUL BOMBAY

AMCONSUL CALCUTTA

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TAGS: EFIN, IN

SUBJ: INDIAN BUDGET FOR IFY 1974/75

REF: NEW DELHI 2842

SUMMARY: BUDGET FOR IFY 1974-75 INCLUDES SHARP INCREASE IN
EXCISE TAXES, MARGINAL CUTS IN INCOME TAX AND REORIENTATION
OF EXPENDITURES AWAY FROM SOCIAL SERVICES TOWARDS CORE SECTORS.
BUDGET POSTULATES SMALL DEFICIT BUT THIS IS EXPECTED TO GROW
SUBSTANTIALLY DURING THE YEAR. AS A RESULT, GOVERNMENT SPENDING
IS EXPECTED TO CONTINUE TO BE A MAJOR SOURCE OF INFLATIONARY
PRESSURE IN INDIA. END SUMMARY.

1. FINANCE MINISTER CHAVAN PRESENTED THE INDIAN CENTRAL
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GOVERNMENT BUDGET FOR IFY 1974/75 ON FEBRUARY 28 TO AN IMPASSIVE

AND GENERALLY SILENT PARLIAMENT. TOTAL EXPENDITURES IN FY 1974/75 ARE ESTIMATED TO BE RS 88.6 BILLION FOR AN INCREASE OF 16.2 PERCENT OVER INITIAL BUDGET ESTIMATES IN IFY 1973/74. DEFENSE EXPENDITURES ARE UP 19.7 PERCENT OVER THE INITIAL 1973/74 BUDGET AND WILL CONSTITUTE 22 PERCENT OF TOTAL CENTRAL GOVERNMENT EXPENDITURES IN 1974/75. REVENUE IS ESTIMATED AT RS 87.4 BILLION.

2. AS THE FIRST ANNUAL BUDGET IN INDIA'S FIFTH FIVE YEAR PLAN, THE IFY 1974/75 BUDGET MIGHT HAVE BEEN EXPECTED TO SET THE STAGE FOR A MAJOR ATTACK ON INDIA'S PRIMARY ECONOMIC PROBLEMS OF UNABATED HIGH INFLATION. ALTHOUGH THE GOVERNMENT RECOGNIZES THAT GOVERNMENT DEFICIT FINANCING WAS A PRIME CAUSE OF THE RECORD INCREASE IN WHOLESALE PRICES AND MONEY SUPPLY DURING 1973/74 THE NEW BUDGET DOES NOTHING TO CHANGE THE SITUATION. WHILE IT COULD JUSTIFIABLY BE ARGUED ON ECONOMIC GROUNDS THAT THE NEW BUDGET SHOULD BE CONTRACTIONARY, THE BUDGET IS IN FACT EXPANSIONARY. WHILE WE RECOGNIZE THAT SUCH A STEP WOULD BE EXTREMELY DIFFICULT POLITICALLY, THE FACT REMAINS THAT THE PRESENT BUDGET WILL CONTRIBUTE SIGNIFICANTLY TO A CONTINUED AND RAPID INCREASE IN MONEY SUPPLY AND WHOLESALE PRICES IN 1974/75.

3. FINANCE MINISTER CHAVAN HAS DISREGARDED THE PLANNING COMMISSIONS RECOMMENDATION THAT THERE BE NO DEFICIT FINANCING DURING THE FIRST TWO YEARS OF THE FIFTH PLAN AND HAS PROVIDED FOR AN ESTIMATED OVERALL DEFICIT OF RS 1.25 BILLION. WHEN IT IS CONSIDERED THAT THE BUDGET DEFICIT FOR THE PRESENT FISCAL YEAR IS NOW ESTIMATED BY MINISTER CHAVAN AT RS 6.5 BILLION INSTEAD OF THE RS 0.9 BILLION HE ESTIMATED LAST FEBRUARY, AND THAT THIS FIGURE WILL PROBABLY BE EVEN HIGHER WHEN THE BOOKS ARE FINALLY CLOSED ON IFY 1973/74, THERE IS VERY LITTLE SOLACE TO BE TAKEN FOR PEOPLE ADVOCATING FISCAL RESTRAINT THIS YEAR.

4. PLAN EXPENDITURES IN IFY 1974/75 AT BOTH THE CENTER AND STATE LEVELS ARE ESTIMATED AT RS 47.7 BILLION COMPARED WITH RS 43.6 BILLION BUDGETED FOR THE CURRENT FISCAL YEAR. ALTHOUGH THE DECLARED OBJECTIVE OF THE PLAN IS TO MOVE FASTER TOWARD LIMITED OFFICIAL USE

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REMOVAL OF POVERTY AND ACHIEVEMENT OF ECONOMIC SELF-RELIANCE, THE BUDGET PUTS RELATIVELY GREATER STRESS ON INCREASES IN COAL TECHNOLOGY AND ON STEEL, FERROUS METAL AND POWER OUTPUT AND RELATIVELY LESS STRESS ON INCREASES IN AGRICULTURE AND SOCIAL AND COMMUNITY SERVICES. IMPORTANT REALLOCATIONS FOR INDUSTRIAL DEVELOPMENT INCLUDE A THREE-FOLD INCREASE IN INVESTMENT IN THE COAL INDUSTRY TO RS 1 BILLION. OF CENTRAL GOVERNMENT EXPENDITURES UNDER THE PLAN, 12 PERCENT IS FOR AGRICULTURE, 35 PERCENT FOR

INDUSTRY, 6 PERCENT FOR POWER, 30 PERCENT FOR TRANSPORT AND COMMUNICATIONS, AND 17 PERCENT FOR SOCIAL AND COMMUNITY SERVICES. WHILE THE SOCIAL WELFARE BUDGET WAS SHARPLY REDUCED FROM THE PREVIOUS YEAR, THE AMOUNT ALLOCATED TO FAMILY PLANNING REMAINS THE SAME.

5. DEFENSE EXPENDITURES IN 1974/75 ARE BUDGETED AT RS 19.2 BILLION, OR 22 PERCENT OF THE TOTAL BUDGET. THIS COMPARES WITH THE 1973/74 INITIAL BUDGET ESTIMATE OF RS 16.00 BILLION AND A REVISED ESTIMATE OF RS 17.5 BILLION. THE FINANCE MINISTER EXPLAINED THAT THE PRINCIPAL REASON FOR THE INCREASE WAS HIGHER PERSONNEL COSTS. IN 1974/75, NEARLY 65 PERCENT OF THE TOTAL DEFENSE EXPENDITURE IS ALLOCATED FOR THE ARMY, 20 PERCENT FOR THE AIR FORCE, 6 PERCENT FOR THE NAVY, AND 9 PERCENT FOR PENSIONS AND OTHER GENERAL ADMINISTRATIVE COSTS.

6. THE BUDGET PROPOSES SEVERAL CHANGES IN THE TAX LAW. EXCISE LEVIES ARE TO BE INCREASED ON A WIDE RANGE OF CONSUMER PRODUCTS GENERALLY PURCHASED BY THE MIDDLE AND UPPER CLASSES SUCH AS TV SETS, AUTOMOBILES AND SCOOTERS. THE MARGINAL TAX RATE ON PERSONAL INCOME OVER RS 70,000 IS TO BE REDUCED FROM 97.75 PERCENT TO 77 PERCENT. FINANCE MINISTER CHAVAN'S ASSERTION THAT THE GOVERNMENT WOULD SUFFER NO REVENUE LOSS AS A RESULT SINCE LOWER PERSONAL INCOME TAX RATES WILL ENCOURAGE LESS EVASION, REMAINS, HOWEVER, TO BE SEEN. THERE WILL BE FEW CHANGES IN CUSTOMS DUTIES OR CORPORATE TAXES IN 1974/75 A TAX REBATE FOR SWITCHES FROM OIL TO COAL FOR INDUSTRIAL USERS WAS SEEN AS A WELCOME MOVE FOR USE OF THE CARROT INSTEAD OF THE STICK ON PRIVATE BUSINESS. TH
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7. UNDER THE PRESENT BUDGET, CENTRAL GOVERNMENT SUPPORT TO THE STATES WILL DECLINE BY RS 3 BILLION FROM CURRENT YEAR LEVELS. SINCE WE DON'T EXPECT THE STATES TO CHANGE THEIR LONG STANDING POLICY AGAINST IMPOSING TAXES ON AGRICULTURAL INCOME (A STATE PREROGATIVE) THE STATES WILL PROBABLY FIND THEMSELVES SIGNIFICANTLY SHORT OF FUNDS NEXT YEAR. THIS, IN TURN, WILL PROBABLY NECESSITATE ADDITIONAL TRANSFERS FROM THE CENTER AS THE YEAR PROGRESSES, SUBSTANTIALLY INCREASING THE GOI CENTRAL BUDGET GOVERNMENT DURING THE COURSE OF THE YEAR.

8. INDIAN PRESS AND PUBLIC COMMENT: THE NEW DELHI FINANCIAL EXPRESS DESCRIBED IT "A SENSIBLE BUDGET" AND COMMENTED THE FINANCE MINISTER FOR HIS "FISCAL BALANCING ACT" BY RAISING RESOURCES WHILE OFFERING RELIEF ON PERSONAL INCOME TAXES. THE TIMES OF INDIA DESCRIBED THE BUDGET AS "PAINLESS" AND NOTED
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THAT INCREASED EXCISE DUTIES HAVE BEEN LEVIED LARGELY ON SUCH COMMODITIES CONSUMED BY THE WALTHIER SECTIONS OF SOCIETY. THE HINDUSTAN TIMES EDITORIAL CRITICALLY NOTES THAT ONCE AGAIN THE DEFICIT HAS BEEN LEFT UNCOVERED. IT STATES THAT THE GOI DEFICIT, COUPLED WITH THE STATES DEFICIT "IS GOING TO FUEL FURTHER THE INFLATIONARY FORCES ALREADY ACTIVE IN THE ECONOMY". THE BUSINESS COMMUNITY REACTED FAVORABLY TO THE PROPOSALS WHICH, CONTRARY TO GENERAL SPECULATION, MAKE NO SUBSTANTIAL UPWARD REVISION OF CORPORATE TAX RATES.

9. COMMENT: OUR OVERALL REACTION IS (1) THE BUDGET WILL BE A MAIN CONTRIBUTING FACTOR TO CONTINUED LARGE INCREASES IN MONEY SUPPLY AND WHOLESALE PRICES IN 1974/75. AS SUCH THE GOVERNMENT HAS MISSED AN IMPORTANT OPPORTUNITY TO ATTACK THE INFLATION PROBLEM. (2) THE BUDGET IS, HOWEVER, A GENERALLY MORE REALISTIC DOCUMENT THAN PREVIOUS FINANCE MINISTRY EFFORTS. EMPHASIS HAS BEEN DIRECTED TOWARD THE CORE SECTORS OF THE ECONOMY (COAL, STEEL, POWER, RAILROADS) AND AWAY FROM SOCIAL WELFARE PLANS.
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